

Strathclyde Pension Fund

Annual Audit Plan 2016/17



 AUDIT SCOTLAND

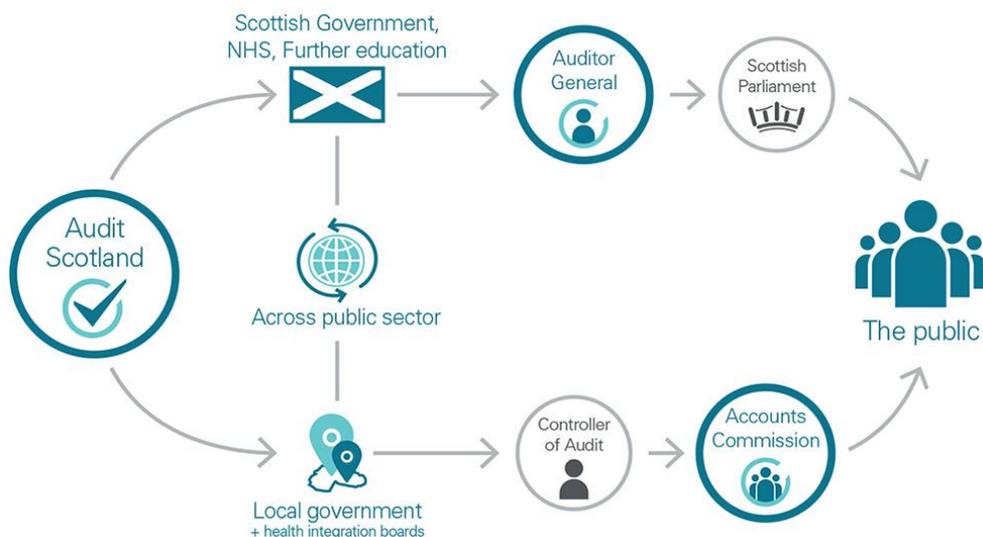
Prepared for Members of Strathclyde Pension Committee

February 2017

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

Contents

| | |
|-------------------------------|----------|
| Risks and planned work | 4 |
| Audit risks | 4 |
| Reporting arrangements | 6 |
| Audit fee | 6 |
| Responsibilities | 7 |
| | |
| Audit scope and timing | 8 |
| Financial statements | 8 |
| Internal audit | 10 |
| Audit dimensions | 11 |
| Quality control | 12 |

Risks and planned work

1. This annual audit plan contains an overview of the planned scope and timing of our audit and is carried out in accordance with International Standards on Auditing (ISAs), the [Code of Audit Practice](#), and any other relevant guidance. This plan identifies our audit work to provide an opinion on the financial statements and related matters and meet the wider scope requirements of public sector audit. The wider scope of public audit contributes to conclusions on the appropriateness, effectiveness and impact of corporate governance, performance management arrangements and financial sustainability.

Audit risks

2. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main risk areas for Strathclyde Pension Fund. We have categorised these risks into financial risks and wider dimension risks. The key audit risks, which require specific audit testing, are detailed in [Exhibit 1](#).

Exhibit 1

| Audit Risk | Management assurance | Planned audit work |
|---|--|--|
| Financial statement issues and risks | | |
| <p>1 Risk of management override of controls</p> <p>ISA 240 requires that audit work is planned to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls in order to change the position disclosed in the financial statements.</p> | <p>Owing to the nature of this risk, assurances from management are not applicable.</p> | <p>Detailed testing of journal entries.</p> <p>Review of accounting estimates.</p> <p>Evaluation of significant transactions that are outside the normal course of business.</p> |
| <p>2 Risk of fraud over income and expenditure</p> <p>ISA 240 presumes a risk of fraud over income which is expanded to include fraud over expenditure in the public sector by the Code of Audit Practice</p> <p>Strathclyde Pension Fund receives a significant amount of investment income from third party sources. This presents a risk due to the extent and complexity of income.</p> <p>The Pension Fund also makes a</p> | <p>Collection of investment income is outsourced to the Fund's global custodian, Northern Trust as an integral part of their asset servicing responsibilities. Northern Trust has resource, systems, and controls designed to manage the complexity of this process across a global investment base.</p> | <p>Evaluating the effectiveness of systems for income recognition and recording.</p> <p>Analytical procedures on income and expenditure streams.</p> <p>Agree income to third party confirmation.</p> <p>Substantive testing of expenditure.</p> |

| Audit Risk | Management assurance | Planned audit work |
|--|---|--|
| <p>range of high value payments, which can constitute a risk of misstatement of expenditure.</p> | <p>System and other internal controls are in place and are subject to internal audit.</p> | |
| <p>3 Estimation and judgements</p> <p>There is a significant degree of subjectivity in the measurement and valuation of investments.</p> <p>This includes level 3 investments such as unquoted equity where valuations use techniques that require significant judgement in determining appropriate assumptions.</p> <p>This subjectivity represents an increased risk of misstatement in the financial statements.</p> | <p>The majority of investments are listed and traded on public stock exchanges which provide frequent valuations.</p> <p>Unquoted investments are valued by third parties including investment managers and independent valuers who follow detailed professional, accounting and industry codes and guidelines.</p> | <p>Completion of 'review of the work of an expert' in accordance with ISA500 for the professional valuer.</p> <p>Test valuations to valuation reports and/or other supporting documentation.</p> |
| <p>4 Changes to financial reporting</p> <p>There are changes to the accounting code for the 2016/17 financial statements:</p> <ul style="list-style-type: none"> • presentational changes to the format of the fund account. • application of IFRS 13 Fair value measurement has been applied to pension fund investments • new recommended disclosures in respect of management expenses. <p>There is a risk that these changes are not properly reflected in 2016/17 financial statements presented for audit.</p> | <p>The new disclosures in respect of management expenses were adopted in the Fund's 2015/16 financial statements.</p> <p>Other changes will be implemented as necessary.</p> <p>Professionally qualified staff keep abreast of financial reporting changes through attending CIPFA training events, consultations, CIPFA publications and CPD.</p> | <p>Communication with officers on the technical details of the changes.</p> <p>Review disclosures as part of our financial statements audit.</p> |
| <p>Wider dimension risks</p> | | |
| <p>5 Financial sustainability</p> <p>The Fund reported a deficit in dealings with members in 2015/16. The cash flow projection for 2016/17 shows a continuing deficit position, which will be funded through use of investment income. Although the medium term projection is for move back to a positive cashflow, there is a risk that the continued increase in pensioners will make funding pension payments increasingly challenging.</p> | <p>Updated cash flow projections show a more positive position.</p> <p>Funding pensions from investment income is a business as usual activity for many funds.</p> <p>The Fund's cash flow forecasting, monitoring and reporting procedures are well established and continue to be developed.</p> <p>The Fund's investment strategy has been adapted to recognise the maturing liability profile and changing cash flow.</p> | <p>Review the financial position of the Fund and the quality of the financial reporting.</p> <p>Monitoring of cash flow forecasting.</p> |

| Audit Risk | Management assurance | Planned audit work |
|--|--|--|
| <p>6 Local government elections</p> <p>The 2017 local government elections will result in changes in the elected members. There is a risk that there is a loss of skills and experience amongst members. To ensure members understand their roles and have the necessary skills to make informed decisions and provide effective scrutiny, development and training will be required. The Audit Scotland publication How Councils Work on the role of councillors provides guidance in this area:</p> | <p>A training plan for Strathclyde Pension Fund Committee members will be developed to complement the Council's induction and training activity.</p> | <p>Review the arrangements for the induction and training of new members.</p> <p>Follow up work on our 2011 national report on the role of boards.</p> |

Reporting arrangements

3. Audit reporting is the visible output for the annual audit. All annual audit plans and the outputs as detailed in [Exhibit 2](#), and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

4. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the Director of Strathclyde Pension Fund to confirm factual accuracy.

5. We will provide an independent auditor's report to Strathclyde Pension Fund and the Accounts Commission summarising the results of the audit of the annual accounts. We will provide the administering authority's Executive Director of Financial Services and the Accounts Commission with an annual report on the audit containing observations and recommendations on significant matters which have arisen in the course of the audit.

Exhibit 2

2016/17 Audit outputs

| Audit Output | Target date | Committee Date |
|--|-----------------|----------------------|
| Interim Audit Report | 30 June 2017 | June 2017 (TBC) |
| Annual Audit Report including ISA 260 requirements | By 30 Sept 2017 | September 2017 (TBC) |
| Signed Independent Auditor's Report | By 30 Sept 2017 | September 2017 (TBC) |

Audit fee

6. The proposed audit fee for the 2016/17 audit of Strathclyde Pension Fund is £53,450. In determining the audit fee we have taken account of the risk exposure of Strathclyde Pension Fund, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit

approach assumes receipt of the unaudited financial statements, with a complete working papers package, by 30 June 2017.

7. Where our audit cannot proceed as planned through, for example, late receipt of unaudited financial statements or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises outwith our planned audit activity.

Responsibilities

Strathclyde Pension Fund Committee

8. Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.

9. The audit of the financial statements does not relieve management or the Strathclyde Pension Fund Committee, as those charged with governance, of their responsibilities.

Appointed auditor

10. Our responsibilities as independent auditor are established by the Public 1973 Act for local government, the Code of Audit Practice, and guided by the auditing profession's ethical guidance.

11. Auditors in the public sector give an independent opinion on the financial statements. We also review and report on the arrangements within the audited body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

Audit scope and timing

Financial statements

12. The statutory financial statements audit will be the foundation and source for the majority of the audit work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the business of Strathclyde Pension Fund and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how Strathclyde Pension Fund will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free of material misstatement.

13. We will give an opinion on the financial statements as to whether they:

- give a true and fair of the financial transactions of the Fund during the year ended 31 March 2017 and the amount and disposition as at that date of its assets and liabilities
- have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union, as interpreted and adapted by the Code of Practice on Local Authority Accounting in the UK
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

Materiality

14. Materiality defines the maximum error that we are prepared to accept and still conclude that that our audit objective has been achieved. It helps assist our planning of the audit and allows us to assess the impact of any audit adjustments on the financial statements.

15. The calculated materiality values for Strathclyde Pension Fund are set out in [Exhibit 3](#).



Exhibit 3

Materiality values

| Materiality level | Amount |
|---|---------------------------------|
| Planning materiality | |
| This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. For the net assets statement it has been set at 0.5% of net assets for the year ended 31 March 2017 based on the latest audited accounts. | Fund No.1 £80.293 million |
| | Fund No.3 £0.918 million |
| Performance materiality | |
| This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement we have calculated performance materiality at 80% of planning materiality. | Fund No.1 £64.234 million |
| | Fund No.3 £0.735 million |
| Reporting threshold - We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at 1% of planning materiality. (with a maximum level of £100,000) | Fund No.1 £100,000 |
| | Fund No.3 £10,000 |

16. When establishing the audit approach, materiality for the financial statements is determined as a whole. However in certain circumstances it is appropriate to apply a lower level of materiality to one or more particular classes of transactions, account balances or disclosures, where misstatements of lesser amounts could influence the economic decisions of users taken on the basis of the financial statements. In the case of a pension fund this applies to member contributions and pensions payments and therefore we will use a lower materiality level when assessing these income and expenditure streams.

17. We review and report on other information published with the financial statements including the management commentary and annual governance statement. Any issue identified will be reported to the Strathclyde Pension Fund Committee.

Timetable

18. To support the efficient use of resources it is critical that a financial statements timetable is agreed with us for the production of the unaudited accounts. An agreed timetable is included at [Exhibit 4](#) which takes account of submission requirements and planned Strathclyde Pension Fund Committee meeting.

Exhibit 4

Financial statements timetable

|  Key stage |  Date |
|---|--|
| Consideration of unaudited financial statements by those charged with governance | By 31 August 2017 |
| Latest submission date of unaudited financial statements with complete working papers package | 30 June 2017 |
| Latest date for final clearance meeting with Executive Director of Financial Services | TBC |
| Agreement of audited unsigned financial statements; Issue of Annual Audit Report including ISA 260 report to those charged with governance | By 30 September 2017 |
| Independent auditor's report signed | By 30 September 2017 |

Internal audit

19. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to rely on the work of internal audit wherever possible and as part of our planning process we carry out an assessment of the internal audit function. Internal audit is provided by Glasgow City Council internal audit overseen by the Head of Audit and Inspection.

Adequacy of internal audit

20. We seek to rely on the work of internal audit wherever possible and as part of our planning process we carried out an early assessment of the internal audit function and concluded that it has sound documentation standards and reporting procedures in place and complies with the main requirements of the Public Sector Internal Audit Standards (PSIAS).

Areas of reliance

21. To support our audit opinion on the financial statements, we plan to place formal reliance on the internal audit review of investments.

22. In respect of our wider dimension audit responsibilities we plan to consider other areas of internal audit work including:

- career average scheme
- review of governance arrangements including compliance with pensions regulator requirements
- fund assurance mapping
- I-connect.

Audit dimensions

23. Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 5](#).

Exhibit 5

Audit dimensions



24. In the local government sector, the appointed auditor's annual conclusions on these four dimensions will contribute to an overall assessment and assurance on best value.

Financial sustainability

25. As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on the fund's financial sustainability in the longer term. We define this as medium term (two to five years) and longer term (longer than five years) sustainability. We will carry out work and conclude on:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability in the short, medium and long term
- the appropriateness and effectiveness of arrangements in place to address any identified funding gaps.

Financial management

26. Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. We will review, conclude and report on:

- whether the Fund has arrangements in place to ensure systems of internal control are operating effectively
- whether the Fund can demonstrate the effectiveness of budgetary control system in communicating accurate and timely financial performance
- how the Fund has assured itself that its financial capacity and skills are appropriate

- whether the Fund has established appropriate and effective arrangements for the prevention and detection of fraud and corruption.

Governance and transparency

27. Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making and transparent reporting of financial and performance information. We will review, conclude and report on:

- Whether the Fund can demonstrate that the governance arrangements in place are appropriate and operating effectively
- whether there is effective scrutiny, challenge and transparency on the decision-making and finance and performance reports
- the quality and timeliness of financial and performance reporting.

Value for money

28. Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on whether the Fund can provide evidence that it is demonstrating value for money in the use of its resources, has a focus on improvement and that there is a clear link to the outcomes delivered.

Independence and objectivity

29. Auditors appointed by Audit Scotland must comply with the Code of Audit Practice. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has in place robust arrangements to ensure compliance with these standards including an annual “fit and proper” declaration for all members of staff. The arrangements are overseen by the Assistant Auditor General, who serves as Audit Scotland’s Ethics Partner.

30. The engagement lead for Strathclyde Pension Fund is Dave McConnell, Assistant Director of Audit. Auditing and ethical standards require Audit Scotland to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of Strathclyde Pension Fund.

Quality control

31. International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor’s report or opinion is appropriate in the circumstances.

32. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland conducts peer reviews, internal quality reviews and is currently reviewing the arrangements for external quality reviews.

33. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time and this may be directed to the engagement lead.

Strathclyde Pension Fund

Annual Audit Plan 2016/17

If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or info@audit-scotland.gov.uk

For the latest news, reports and updates, follow us on:



Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
T: 0131 625 1500 E: info@audit-scotland.gov.uk
www.audit-scotland.gov.uk